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# INTELLIGENCE BRIEF

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Review of this document by CIA has determined that

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☐ It contains nothing of CIA Interest

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## ECONOMIC "CRISIS" IN IRAN

Iran's impending economic "crisis" is essentially a bookkeeping difficulty. Although the magnitude of the fundamental and long term problem of the Iranian economy cannot be overstated, the situation immediately ahead and, indeed, for a considerable period into the future, is one that can readily be met by a willingness on the part of the government to pursue unorthodox -- for Iran -- fiscal and monetary policies. In this situation, emergency foreign assistance is not of direct economic relevance.

The paramount economic problems posed for Iran by the loss of the revenues formerly accruing from the operations of the Anglo-Iranian Oil Company are twofold: the foreign exchange problem and the domestic fiscal problem.

On the foreign exchange side, Iran abandoned the equivalent of approximately \$100,000,000 annually when it forced the AIOC to suspend operations. To date, the effect of this loss on the Iranian economy has been slight and indirect. Imports of essential commodities apparently have not been reduced appreciably, wholesale and retail prices have remained relatively stable, and no important new hardships have been inflicted on the mass of the Iranian population. The drain on Iran's exchange holdings appears to have been limited in extent if, in fact, there has been any drain at all. Import cuts have been forced by the partial UK freeze on the use of Iranian-held sterling and by mild administrative measures taken in Iran. Far greater austerity is possible as regards imports; with exports at present high levels, it might be possible for Iran to eliminate the small trade deficit that may exist.

Iran's fiscal operations have been somewhat more seriously affected. In Iran, doctrines of monetary orthodoxy have dominated governmental thinking to an uncommon degree. Prior to the withdrawal of the AIOC, Iranian Governments had counted on receipt of royalty payments in sterling which could be sold to the Central Bank for currency to cover a portion of the governmental pay rolls. Normally, these receipts, plus ordinary revenues, made it possible to cover governmental expenses. When, as has happened from time to time, the government could not obtain sufficient sums from these sources, payments to the bureaucracy and the army were simply delayed. (Cont'd on next page.)

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legend. All this was well within the limits of the prevailing orthodox views on fiscal-monetary policy.

3-1 With the end of AECG payments, Khomeini's government took the bold step of ~~seeking~~ and getting legislative assent to the transfer to current government account of \$30,000,000 from the hitherto sacrosanct currency reserve. This sum, plus \$5,500,000 loaned to Iran by the International Monetary Fund, has been sold to the Central Bank for currency needed to meet government expenses. Within the next six or eight weeks, when these funds will have been exhausted, the Government of Iran will be technically bankrupt in the sense that ordinary revenues will fall short by about the equivalent of \$10,000,000 a month, covering total government expenses.

The size of the deficit, however, should not obscure the actual nature of these transactions. The sums that the government has "expended" were first transferred on the books of the Central Bank to government account and then transferred back to Central Bank account. Only a fraction of the total amount — almost certainly not more than \$10,000,000 and perhaps much less — was sold by the Bank to exporters or used by the government for foreign purchases and thus removed from the Iranian economy. And this episode draws to a close, the Iranian Government has been able to meet its obligations, including payments to the unemployed workers in the oil fields, in a satisfactory fashion. No particularly serious consequences have followed from this venture into monetary heterodoxy and Iran's total foreign exchange holdings (which potentially include the gold held against currency issues) have not been reduced enough to warrant serious concern.

The present government — or its predecessor — has a range of means open for dealing with its imminent "bankruptcy." It can ask the Mullis to transfer another allotment of the currency reserve to current government account and begin again the procedure of selling this amount to the Central Bank for rials. It can seek to have the currency issue ceiling lifted and the power of the government to borrow from the Central Bank expanded. It can undertake the flotation of the "national loan" that was announced months ago and, by mixing appeals to patriotic sentiment with the judicious use of terror, perhaps realize sizable sums. It can attempt to raise tax rates and tighten collection mechanisms, although this effort obviously could not bring quick and large results. Any single one of these measures or a combination of them would require a certain amount of political will and courage, given Iranian devotion to "sound banking" for its currency. Under present circumstances, none, except perhaps effective tax collections, need be politically impossible unless, for other reasons, the government has lost its popular support. Objectively, none involves short-term economic hazards of any great magnitude.

It is quite true that foreign aid of a sufficiently stringless nature might provide a politically painless solution. And, if the government chose to spend the proceeds of such foreign aid on imports, it could

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either do something toward economic development or increase the quantities of consumption goods available in Iran, or something of both. These possibilities, however, are not related to the immediate issue. The Iranian Government could in effect merely bank the proceeds, choosing not to exercise its added claims to foreign goods, and not be particularly the worse off for its choice. Its present problem, in other words, is not one of inadequate resources but rather one of finding a politically palatable bookkeeping technique. Foreign assistance for "budgetary" purposes would be such a technique but it can scarcely be considered as necessarily the only one.

In the final test, of course, the problem facing the Iranian Government is a political one. If it proves unable or unwilling to accept whatever political risks the requisite domestic monetary and fiscal measures would entail, and if, in these circumstances, no foreign aid were forthcoming, then it would in fact be bankrupt. The consequences within Iran are not foreseeable in detail but they could not be pleasant.

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